The Internal Revenue Service Needs to Improve the Pre-Filing Tax Services Provided to Taxpayers

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DEPARTMENT OF THE TREASURY

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INSPECTOR GENERAL
for TAX
ADMINISTRATION

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MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

FROM: Pamela J. Gardiner
Acting Inspector General

SUBJECT: Final Audit Report - The Internal Revenue Service Needs to Improve the Pre-Filing Tax Services Provided to Taxpayers (Audit # 200140049)

This report presents the results of our review to determine if implementation of the Internal Revenue Service's (IRS) Stakeholder Partnerships, Education, and Communication (SPEC) function is meeting implementation timelines and standards to enable the function to effectively ensure taxpayers are provided the information, support, and assistance they need to understand and fulfill their tax obligations.

The goal of IRS redesign efforts for the Wage and Investment (W&I) Division was to build a new organizational structure that provides more education and assistance to W&I taxpayers to enable them to better understand and satisfy their tax responsibilities. The IRS noted in its W&I redesign plans that in going forward the IRS will place more emphasis on *pre-filing* activities – addressing taxpayer problems early in the process rather than well after tax returns have been filed.

The taxpayers served by the W&I Division are highly compliant with tax filing requirements and typically file simple tax returns. Many of the tax problems faced by W&I taxpayers have less to do with tax evasion and more to do with a misunderstanding of their tax obligations due to education and communication issues. The IRS' SPEC function is responsible for proactively serving the *pre-filing* service needs of W&I taxpayers.

Our review identified that the IRS has not successfully made the shift from addressing taxpayer problems well after tax returns are filed to addressing problems early in the tax process to prevent them when possible, which is one of the overriding themes of improving the IRS' business practices. Key operational deficiencies have resulted in the IRS' lack of ability to meet the SPEC function's implementation milestones and have significantly affected the ability of the IRS to provide taxpayers with expanded and improved *pre-filing* tax services. Key operational deficiencies identified include (1) SPEC field offices lacked adequate staffing and managerial oversight, (2) employees in field offices had not received mission critical training and/or had not met professional requirements, (3) computer equipment was not adequate to support the IRS' volunteer tax assistance programs, and (4) performance/management systems had not been developed to monitor and measure the impact SPEC activities have on improving tax compliance.

Unless these operational deficiencies are addressed, particularly those that affect the volunteer tax assistance programs, taxpayers will not receive the improved *pre-filing* tax assistance to which the IRS has publicly committed. In addition, the IRS will not be able to support a key strategy of reducing the volume of taxpayers it serves in its walk-in tax assistance sites by expanding the number of volunteer sites. However, the IRS is in the business of processing tax returns and collecting tax revenue within the constraints of a budget provided by the Congress. The allocation of the budget by IRS executives supports the position that tax return processing and the collection of tax revenue are priorities. A significant shift of funding away from *filing* and *post-filing* activities to *pre-filing* activities is unlikely. A significant budgetary shift seems even more unlikely until the impact of *pre-filing* activities on the improvement in taxpayer behavior can be measured.

<u>Management's Response</u>: IRS management acknowledged that the SPEC organization represents a new vision in *pre-filing* service delivery for the IRS. Management stated that, "While your report accurately points out that much of the operational infrastructure necessary to implement and manage the new SPEC business model was not in place at stand up, it does not adequately take into account the operational complexities of actually putting the new model into practice." They also stated, "Understandably, initiation of a comprehensive review of a new organization 1 year after it was created would identify significant inherited deficiencies. As a result, subsequent events have superseded many of the findings in your report."

Management felt that our conclusion that the lack of staffing had a negative impact on the numbers of taxpayers assisted was an example supporting their opinion. They believe that, since we did not capture accomplishments for an entire fiscal year, our report inaccurately shows that the number of taxpayers assisted decreased in FY 2002 relative to the past 2 years.

Similarly, the IRS believes that ongoing developments show its operational capabilities (such as information management systems, performance measures, and training) are improving. The IRS provided specific comments to each of the key operational deficiency areas we reported. Management's complete response to the draft report is included as Appendix VI.

<u>Office of Audit Comment</u>: Due to the time frame of our audit, we can draw no conclusions about events that occurred after the audit ended. Figures shown in our report were accurate as of the end of our audit. We did not make recommendations in this report and do not intend to elevate our disagreement concerning this matter to the Department of the Treasury for resolution.

Copies of this report are also being sent to the IRS managers who are affected by the report. Please contact me at (202) 622-6510 if you have questions or Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 927-0597.

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Background

In 1998, the Congress passed the Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)[1] directing the IRS to reorganize its operations. In response to the RRA 98, the IRS reorganized into four business divisions[2] based on taxpayer needs. One of the four business divisions is the Wage and Investment (W&I) Division, which began operation in October 2000. The W&I Division serves approximately 116 million taxpayers filing approximately 90 million tax returns.

The goal of the W&I Division redesign efforts was to build a new organizational structure that provides more education and assistance to W&I taxpayers to enable them to better understand and satisfy their tax responsibilities. The taxpayers served by the W&I Division are highly compliant with tax filing requirements and typically file simple tax returns. Many of the tax problems faced by W&I taxpayers have less to do with tax evasion and more to do with a misunderstanding of their tax obligations due to education and communication issues.

The W&I Division is organized into three broad categories of activities that coincide with the following three stages of an individual taxpayer's interaction with the IRS:

- *Pre-filing* – educating and assisting taxpayers before their tax returns are filed, including providing taxpayers with the information, support, and assistance they need in order to understand and fulfill their tax obligations. Oversight is provided by the Customer Assistance, Relationships, and Education (CARE) function.
- *Filing* – processing tax returns. Oversight is provided by the Customer Account Services function.

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[1] Pub. L. No. 105-206, 112 Stat. 685.
[2] The four business divisions include W&I, Large and Mid-Size Business, Small Business/Self-Employed, and Tax Exempt and Government Entities.

- *Post-filing* – working with taxpayers who have not filed their required tax returns, have a delinquent tax payment, or have an audit issue. Oversight is provided by the Compliance function.

The IRS noted in its W&I Division design plans that, in going forward with the W&I Division, the IRS will place more emphasis on *pre-filing* activities – addressing taxpayer problems early in the process rather than well after tax returns have been filed.

Within the CARE function is the IRS' Stakeholder Partnerships, Education, and Communication (SPEC) function. The SPEC function is responsible for proactively serving the *pre-filing* needs of W&I taxpayers. The SPEC function is a blend of the former Taxpayer Education (TPE) and Electronic Tax Administration (ETA) field functions that existed under the IRS prior to its reorganization.

Major responsibilities of the SPEC function include:

- Overseeing the IRS' Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) Programs. The VITA/TCE Programs provide free tax help to people for whom professional assistance may be too expensive. SPEC management estimates that 85 percent of SPEC field resources are expended for the delivery and oversight of the VITA Program alone.
- Focusing educational and assistance efforts on four underserved segments of W&I taxpayers – low-income, elderly, non-English speaking, and disabled.
- Establishing partnerships with community organizations and businesses to assist the IRS in its educational and outreach efforts.
- Developing educational programs, marketing campaigns, etc., to promote IRS programs such as *e-filing* and the Earned Income Tax Credit (EITC).

The majority of the SPEC function's *pre-filing* interaction with W&I taxpayers occurs at the Field Operations Level.

Field offices[3] are responsible for delivering the products of the SPEC function to taxpayers, providing tax return preparation assistance, marketing volunteer-provided services, promoting the IRS' *e-filing* program, and providing back-up assistance at IRS walk-in tax assistance sites. The total operating costs for the SPEC function, exclusive of office space rental, postage, and printing was $45 million for Fiscal Year (FY) 2001 and is projected to be $53 million for FY 2002.

This audit was conducted at the IRS' W&I Division CARE function, the IRS' SPEC Headquarters office, and SPEC field offices from October 2001 to April 2002. The audit was conducted in accordance with *Government Auditing Standards.* Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Operational Deficiencies Have Significantly Affected the Ability to Provide Taxpayers with Expanded and Improved Pre-Filing Tax Services

The IRS has not successfully made the shift from addressing taxpayer problems well after tax returns are filed to addressing these problems early in the tax process to prevent them when possible, which is one of the overriding themes of improving the IRS' business practices. Key operational deficiencies have resulted in the IRS' lack of ability to meet the SPEC function's implementation milestones[4] and have significantly affected the ability of the IRS to provide taxpayers with expanded and improved *pre-filing* tax services.

Key operational deficiencies identified include:

- SPEC field offices lacked adequate staffing and managerial oversight.
- Employees in field offices had not received mission critical training and/or had not met professional requirements.

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[3] The term "field offices" will be used throughout the remainder of this report as reference to those SPEC offices located in proximity to local partner organizations and taxpayers (otherwise referred to as "territory/post of duty" offices).
[4] SPEC function reorganization milestones are included in the W&I Division design plans.

- Computer equipment was not adequate to support the IRS' volunteer tax assistance programs.
- Performance/management systems had not been developed to monitor and measure the impact SPEC activities have on improving tax compliance.

<u>SPEC field offices lacked adequate staffing and managerial oversight</u>

Identification of staffing levels and geographic location of SPEC field offices

The IRS, with the assistance of an outside consultant, analyzed Census Bureau data as well as IRS individual tax return filing data to identify both the geographic locations of the SPEC field offices and the staffing levels needed in these offices. The geographic locations of the field offices were primarily determined by the ability of taxpayers (including the underserved[5] low-income, non-English speaking, elderly, and disabled) to obtain convenient access to these services. The staffing level was directly linked to the number of taxpayers within the commuting area of the field office.[6]

The geographic locations and staffing levels in these locations was included in a formal SPEC Staffing Plan approved by the IRS Commissioner. The Staffing Plan called for 7 area offices (to oversee field offices) and 72 field offices nationwide. Subsequent to the initiation of the SPEC function, an additional 7 field offices were added to accommodate existing IRS employees transferred to the SPEC function from the now defunct TPE and ETA field functions. The 79 field offices were to be managed by 48 managers (see Appendix V). Total recommended staffing in SPEC area offices and field offices is 104 and

[5] Those individuals that cannot reasonably access tax assistance by virtue of their income level, diversity, language, or age and for whom no reasonable alternative assistance is available in the commercial market.
[6] Repeated requests were made to obtain the analysis performed to identify the potential number of taxpayers who could receive benefits; however, the IRS was unable to locate the information supporting this analysis.

697, respectively. The recommended staffing levels are to be in place by October 2002.

Our review identified that the SPEC function will not meet the staffing levels outlined in the Staffing Plan by the target date of October 2002. National SPEC management agreed with our assessment.

Not all field offices have managers

As of March 2002, 7 of the 48 field office managerial positions had not been filled despite the function standing up in October 2000. The vacant territory manager positions are in the following field offices: Albany, New York; Charlotte, North Carolina; Cleveland, Ohio; Columbus, Ohio; Omaha, Nebraska; San Jose, California; and Washington, DC. National SPEC management noted that the primary reason managerial positions have not been filled is that individuals applying for these positions lack the necessary qualifications.

Significant staffing shortages exist in SPEC area and field offices

Significant staffing shortages exist in both SPEC area offices and field offices. The table below outlines the staffing shortages, as of February 2002, in SPEC area offices when compared with the level of staffing presented in the SPEC Staffing Plan.

SPEC Area Office Staffing Shortages

Area Office	Staffing Level as of February 2002	Full Staffing Level per SPEC Staffing Plan
Hartford	6	14
Greensboro	6	17
New Orleans	7	14
Indianapolis	6	14
St. Louis	6	17
Phoenix	5	14
San Diego	3	14
Totals	**39**	**104**

Source: SPEC Staffing Reports dated February 19, 2002.

Of the originally planned 72 field offices, 63 (88 percent) were understaffed as of February 2002 (see Appendix IV for a complete listing of staffing levels in the 72 SPEC field offices). For 29 of the 63 understaffed field offices, staffing levels are 50 percent or more below Staffing Plan levels. In addition, the following six field offices have no staff at all: Burlington, Vermont; Charlotte, North Carolina; Portland, Maine; Providence, Rhode Island; Raleigh-Durham, North Carolina; and Sioux Falls, South Dakota.

Impact of staffing shortages

The SPEC function was created to meet the educational and assistance needs of individual taxpayers, particularly those that have low income and/or are elderly, disabled, or non-English speaking. To assist the IRS in its outreach efforts, the SPEC function was to establish partnerships with local community organizations and businesses. However, the significant lack of staffing, and in some locations no staffing, make it extremely difficult if not impossible to support this initiative. As a result, many taxpayers in the four underserved segments are not receiving the high-quality tax return preparation services free of charge and may not be obtaining the credits (e.g., EITC, child tax credit, etc.) to which they are entitled.

Furthermore, staffing shortages are affecting the SPEC function's ability to deliver the level of *pre-filing* services previously provided under the old TPE and ETA functions. The following table illustrates the decline in key volunteer program measures since SPEC stand-up.

Key Volunteer Program Measures (FY 2000 – FY 2002)

	Pre-SPEC	SPEC			
	FY 2000	**FY 2001**	**% Change from FY 2000**	**FY 2002**	**% Change from FY 2001**
Taxpayers Assisted	3,790,232	3,587,179	**-5%**	3,482,303	**-3%**
Volunteers	79,485	76,018	**-4%**	68,305	**-10%**
Assistance Sites	18,150	18,238	**0%**	14,620	**-20%**

Source: Taxpayer Information and Education Reports (Table 4) provided by the SPEC function.

The impact of staffing shortages will continue to result in a decline in the number of volunteer assistance sites as the SPEC function plans on closing approximately 1,000 volunteer sites nationwide in FY 2003. This continued decline in volunteer sites contradicts the IRS' strategy of reducing the volume of taxpayers it serves in its walk-in tax assistance sites by expanding the number of volunteer sites.

Below are excerpts from responses provided to National SPEC management from field office managers regarding the impact staffing shortages are having on the delivery of the SPEC program:

"The lack of staffing is so pervasive that it can be cited as the basic underlying cause of all difficulties associated with this filing season."

"We have not conducted outreach sessions where we targeted groups of potential EITC recipients. Without staff it is a challenge to have an aggressive outreach program."

"Several factors contributed to the reduction in taxpayers assisted through outreach. The most significant was the reduction in staff, which resulted in a diminishment of experience and expertise."

Employees in field offices had not received mission critical training and/or had not met professional requirements

Implementation of the new SPEC function results in the creation of a new IRS field position

The implementation of the new SPEC function resulted in the creation of a new field employee position, entitled Tax Specialist (TS), with responsibilities that include reviewing and analyzing taxpayer financial statements, preparing income tax returns, providing technical tax law and accounting assistance, providing assistance in presenting seminars and speeches to highlight IRS programs for specific audiences, and assisting in conducting studies and surveys to evaluate marketing programs.

To formulate the professional requirements and the training needs of the new TS position, the SPEC function formed a team of SPEC employees and individuals from the IRS' Learning and Education area. SPEC management prioritized the TS position as the most critical position for development and delivery of training initiatives. For the TS position, the team identified the following training courses to be mission critical:

- *Basic and Advanced Income Tax Law.*
- *Communications.*
- *Stakeholder Relationship Management*.
- *Marketing.*

In addition to the above training, the TS position requires an individual to have 6 or 12 semester hours of accounting credits depending on his/her level of responsibility. The accounting credit requirement is based on the fact that TS responsibilities include assisting taxpayers with accounting methods, practices, and other technical matters.

Individuals newly hired to the SPEC function are required to have the necessary accounting credits. However, for those IRS employees transferring to the SPEC function without the necessary accounting credits, the SPEC function provides these employees 1 year to obtain the credits and online access to the classes necessary to be completed to do so.

The majority of field employees have not met professional requirements and/or have not completed mission critical training

Our review identified that 107 (34 percent) of the 318 TSs, employed by the SPEC function as of February 2002, had not obtained their needed accounting credits to qualify for the position of TS. The SPEC function does not have a system in place to track the progress of employees in meeting accounting credit requirements.

Furthermore, we identified that the majority of the TSs have not received what SPEC management refers to as mission critical training. The table below summarizes the mission critical training received by the 318 TSs employed as of February 2002.

Status of TS Completion of Mission Critical Training

Training Class	Completed Training	Not Completed Training
Basic Income Tax Law	77	241*
Advanced Income Tax Law	0	318
Communications	0	318
Stakeholder Relationship Management	0	318
Marketing	0	318

Source: Information obtained from SPEC Training Coordinator.

** Some of the individuals included in the 241 who have not received Basic Income Tax Law training may in fact have received this training. The individuals who may have received the training are those that transferred to the SPEC function from another IRS function. However, National SPEC management was unable to provide specific information as to the number of individuals transferring into the SPEC function who had previously received Basic Income Tax Law training.*

Impact of inadequate mission critical training

The inability of the IRS to adequately train its employees has been an issue raised by employees as affecting morale. National SPEC management indicated that the lack of training continues to have a dramatic impact on the effectiveness of the SPEC function. The lack of adequate training results in inefficiency and ineffectiveness of the SPEC field office operations. In addition, those employees that do not meet the professional requirements would not advance to the TS position. This would result in a further shortage of tax specialists as well as a possible pool of employees for which there is no business need within the SPEC function.

Computer equipment was not adequate to support the IRS' volunteer tax assistance programs

The majority of SPEC resources support volunteer tax programs

The majority of SPEC resources are devoted to the delivery of the IRS' volunteer income tax assistance programs. National SPEC management estimates that over 85 percent of its field full-time equivalents (FTE)[7] are used to support the volunteer programs.

To enable volunteers to offer taxpayers the option of *e-filing* their tax returns, the IRS provides over 10,000 desktop and laptop computers for use in volunteer tax programs. The computers the IRS provides to its volunteers include the tax preparation software necessary to *e-file* a tax return to the IRS. *E-filing* assists volunteers in more accurately preparing tax returns and allows taxpayers to receive tax refunds quicker than those received for a paper filed tax return. For the 2002 Filing Season, volunteers prepared over 1.1 million tax returns with approximately 768,000 (65 percent[8]) being *e-filed*.

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[7] Each FTE is equal to the total number of compensable hours in a given fiscal year that 1 employee can work, determined by the following simple formula: Total days in a given year, excluding Saturdays and Sundays, times 8 compensable hours per day equals hours per FTE, usually 2,088.
[8] Percentage based on actual figures of 1,178,142 prepared and 767,928 *e-filed*. Rounded numbers used for readability.

Computer equipment necessary to promote e-filing at volunteer sites is significantly lacking

Despite the substantial number of computers provided to the volunteer program, SPEC field offices still significantly lack the computer equipment and technical support needed to deliver the volunteer tax assistance programs. Specifically, the SPEC function estimates that over 4,500[9] additional computers are needed to support the volunteer tax programs. The shortage of computers will become even more critical in that a large percentage of the computers currently in use will be obsolete[10] in the 2002 Filing Season. National SPEC management has indicated that the control and accountability of computers and the estimate of computer needs are areas where significant improvement is needed.[11]

During the SPEC function's first year of operation, SPEC field managers continually reported that computer-related problems (shortages and breakdowns) were seriously hampering their ability to provide *e-filing* at volunteer sites. For example:

"All I am trying to do at this point is keep viable electronic filing sites that operated in the past in business by replacing broken equipment but I am unable to even do that."

"Tax Counseling for the Elderly Program (TCE) lacked sufficient equipment to enable them to fully expand their program…."

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[9] The number of computers needed to support the volunteer programs may be substantially higher because the SPEC function does not have an accurate inventory system to identify what is currently in inventory or a process to accurately determine the needs in each of its offices to support volunteers in that commuting area.

[10] The software necessary to *e-file* will no longer operate on these computers because of the age of the computer as well as the processing speed of the computer.

[11] During the course of this review, auditors identified significant weaknesses relating to the control and accountability over computers provided for use in the IRS' VITA/TCE program. Because of the significance of the control weaknesses identified and the fact that these computers contain taxpayer *e-file* data, a separate report was issued; see *Computers Used to Provide Free Tax Help and That Contain Taxpayer Information Cannot Be Accounted For* (Reference Number 2001-40-144, dated August 2002).

"We need additional computer equipment for our volunteers if we are going to increase e-file. We are juggling equipment from one site to another…."

Volunteers have raised similar concerns regarding the inadequacy of computer equipment. For example:

"Not all sites prepare electronic tax returns at this time. The primary constraint to expansion of e-filing is lack of enough equipment."

In addition to the critical shortage in computers 27 (56 percent) of the 48 field office managers have indicated that needed technical support is not available. Technical support includes delivery and setup of computers at volunteer sites, installation and updates of the necessary software needed to *e-file* tax returns, and troubleshooting and fixing problems with the computers.

The table below presents the results of an e-mail survey the Treasury Inspector General for Tax Administration (TIGTA) performed of the 48 field office managers to determine the number of managers that in their opinion had the needed technical support. (See Appendix V for a complete listing of responses by field office – results by field offices is larger than results by field office managers as managers can often oversee more than one location.)

Field Office Manager Responses – Technical Support

TIGTA Survey Question	Territory Manager Response	
	Yes	No
Does your territory have technical support?	27	21

Source: Responses provided by the territory managers for 48 territories to a TIGTA e-mail survey.

Impact of computer and technical assistance shortages

A recent survey of volunteers involved in the IRS' tax assistance programs indicated that computer equipment is top among their needs, based on their experience during the 2001 Filing Season. Without the needed computers, volunteers are unable to offer *e-file* to taxpayers who use their services. Providing computers to volunteers is one of the most important support needs that the IRS can address and is critical to the success of this program and to the promotion of *e-filing*.

Performance/management systems had not been developed to monitor and measure the impact SPEC activities have on improving tax compliance

The SPEC function does not have the ability to measure the impact of its education and assistance efforts on improving individual taxpayer compliance (ability of taxpayers to understand and satisfy tax responsibilities). Specifically, SPEC management is unable to measure the improved qualitative impact on taxpayers, as well as the quantitative impact that the changing of taxpayer behavior may have on other IRS processes.

When the SPEC function took over operations in October 2000, it inherited many of the measurement problems that still exist today. The measurement systems in place for TPE/ETA field operations were separate systems maintained at each of the 33 district offices nationwide. The information captured was often not consistently recorded or consistent with regard to what was being captured, particularly in the manner in which taxpayer assistance was calculated. Furthermore, there was no ability to measure the impact that TPE/ETA activities had on improving taxpayer compliance.

Although the SPEC function is unable to successfully measure the benefits its activities have on improving compliance, it has made some progress in the development of measurement systems. This progress includes:

- Identifying previous flaws in the counting of taxpayers assisted.
- Attempting to implement a consistent approach to counting taxpayers contacted or assisted through the SPEC function’s various methods of dealing with taxpayers, such as answering taxpayer questions, preparing tax returns, and conducting seminars and direct marketing campaigns.

- Implementing the Partnership Satisfaction Survey, which was developed by the SPEC function to assess volunteer partner satisfaction with SPEC programs, to obtain suggestions for program improvements and to determine the needs of the various partners. The results from the most recent survey are not representative of the population of volunteers the SPEC function is involved with. We identified that, as a result of a restrictive definition of what constitutes a partner, the SPEC function excluded a large population of volunteers that have regularly participated in the IRS volunteer tax assistance programs. When TIGTA auditors brought this to the attention of National SPEC management, the restrictive definition of what constitutes a partner was revised.
- Initiating a project (CARE Benefits Model) in February 2001 to structure and quantify the benefits of *pre-filing* activities on both the IRS and taxpayers. Work is ongoing to build a mechanism to measure the impact SPEC activities have on changing taxpayer behavior and improving taxpayer compliance.

Impact of inadequate measurement systems

Without adequate measurement systems, the SPEC function does not have the ability to measure the value of its proactive programs, which is one of the challenges detailed in the SPEC Design Plan. Furthermore, tracking the effectiveness of the SPEC program is essential as the Congress is interested in the impact the SPEC function has on *post-filing* activities, including decreasing the workload assigned to *post-filing* functions. However, it should be noted that designing this type of measurement system would be extremely difficult. Measuring the impact that *pre-filing* activities has on changing taxpayer behavior is not an immediate and clear measurement, as is the case with IRS *filing* (tax returns filed) and *post-filing* (audits completed, dollars collected) activities.

Contributing factors resulting in the operational deficiencies identified

The majority of the IRS' budget continues to be expended on filing and post-filing activities

Relatively little funding is expended on IRS *pre-filing* activities. Specifically, the IRS continues to expend the majority of its resources on *post-filing* activities. For FYs 2002 and 2003, budget estimates show that on average 6 percent of the IRS' entire budget has been devoted to *pre-filing* activities (see table below).

Resource Allocation Estimates[12] FYs 2002 – 2003

Fiscal Year	*Pre-Filing*	*Filing*	*Post-Filing*
2002	6%	17%	37%
2003	6%	17%	37%

Source: IRS Budget in Brief FYs 2002 and 2003.

In addition, the SPEC function has taken significant cuts to its planned FTE budget. During the SPEC function's first year of operation, FTEs were cut by 34 percent, which resulted in a significant deviation from the Commissioner-approved SPEC Staffing Plan. The 34 percent FTE budget cut, in addition to the continued loss of supporting resources from other IRS functions (see below), significantly affects the SPEC function's ability to meet program goals and objectives.

Resource needs were significantly underestimated when the staffing plan was developed

When the design team was developing the SPEC Staffing Plan, it was unaware of the significant resources provided by IRS functions outside of the TPE and ETA functions at the local level to deliver the various programs that were transferred to the new SPEC function. Specifically, under the old IRS structure the delivery of *pre-filing* programs was the responsibility of local IRS executives. To ensure

[12] The remainder of the budget is allocated to programs such as Business Systems Modernization, Information Technology, etc.

pre-filing programs met their goals, local IRS executives regularly transferred resources from other field functions at the local level.

Subsequent to the initiation of the SPEC function and the start of the 2001 Filing Season, it quickly became evident to SPEC management that the resources transferred at a local level to support the old TPE and ETA programs were significant. SPEC management attempted to quantify the resources previously provided by other IRS functions at a local level.

The SPEC analysis of the limited and incomplete data maintained under the old IRS organization identified that a minimum of approximately 250 FTEs had been transferred from IRS functions outside of the TPE and ETA functions to support the *pre-filing* activities now the responsibility of the SPEC function. These 250 FTEs were not included in the design team's staffing estimates and were not transferred to the SPEC function at the time of stand-up. However, the SPEC function has received some resources from other IRS functions for the 2001 and 2002 Filing Seasons. The SPEC function indicated that no resources will be provided for the 2003 Filing Season and beyond.

Funding and the lack of ability to develop training courses have contributed to SPEC field employees not receiving mission critical training

Training budget requests have been cut significantly for FYs 2001 and 2002, as follows:

Training Budget Cuts – FYs 2001 and 2002

Fiscal Year	Amount Requested	Amount Provided	Percent Not Funded
2001	$2,100,000	$461,910	78%[13]
2002	$3,197,628	$1,815,720	43%

Source: SPEC Training Budget Data.

[13] The impact of this cut was diminished by the fact that staffing shortages resulted in the need to train fewer employees than expected.

Training-related travel accounts for most of the annual training budget ($3,194,070 of the FY 2002 training budget is for individuals to attend the training sessions).

In addition to budgetary constraints, the development of the mission critical training curriculum involves SPEC employees working with the IRS' Learning and Education area. However, the SPEC employees assigned to developing the training curriculum have been unable to perform this task because they are needed to participate in the education and assistance activities during the filing season. As a result, training modules for two mission critical training areas have not been completed.

Management information systems have not been developed to enable SPEC to be a data-driven business

Key operating mechanisms, including centralized national management information systems, have not been developed to allow SPEC management to make informed data-driven business decisions and to monitor those aspects of the SPEC operation that are critical to its success. The SPEC function has not been able to devote adequate resources to the development of these systems. The majority of its resources are expended on sustaining existing programs inherited at the time the SPEC function became operational.

Conclusion

The IRS is in the business of processing tax returns and collecting tax revenue within the constraints of a budget provided by the Congress. The allocation of the budget by IRS executives supports the position that tax return processing and the collection of tax revenue are priorities.

A significant shift of funding away from *filing* and *post-filing* activities to *pre-filing* activities is unlikely. A significant budgetary shift seems even more unlikely until the impact that *pre-filing* activities have on the improvement in taxpayer behavior can be measured. However, unless the operational deficiencies identified during the course of this audit are addressed, particularly those that affect the volunteer tax assistance programs, taxpayers will not receive the improved *pre-filing* tax assistance to which the IRS has publicly committed. Furthermore, the IRS will not be able to support a key strategy of reducing the volume of taxpayers it serves in its walk-in tax assistance sites by expanding the number of volunteer sites.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine if implementation of the Internal Revenue Service's (IRS) Stakeholder Partnership, Education, and Communication (SPEC) function is meeting implementation timelines and standards to enable the function to effectively ensure taxpayers are provided the information, support, and assistance they need to understand and fulfill their tax obligations. Specifically, we:

I. Interviewed SPEC headquarters management to obtain current staffing, training, computer equipment, and supply information and management perception of how any related operational deficiencies may affect taxpayers.

II. Obtained the SPEC Staffing Plan and other key operational guidance and determined if actual staffing, training, computer equipment, and supply allocations meet plans/standards.

III. Determined and evaluated the method followed by the SPEC function for allocating staffing, training, computer equipment, and supplies to priority areas.

IV. Determined the basis for and evaluated business decisions leading to any budget cuts relating to SPEC staffing, training, computer equipment, and supplies by interviewing responsible analysts in both the SPEC and Strategy and Finance functions.

V. Reviewed and analyzed 2001 Filing Season feedback from SPEC offices to identify the extent of any deficiencies/taxpayer impact relating to staffing, training, computer equipment, and supplies and assessed any actions taken to ensure deficiencies are timely corrected.

VI. Interviewed selected area and field office managers and reviewed relative documentation to assess taxpayer impact relating to any operational deficiencies identified.

VII. Assessed the impact that volunteer-based tax assistance efforts have on narrowing any identified operational deficiencies.

Appendix II

Major Contributors to This Report

Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs)
Kerry Kilpatrick, Director
Russell Martin, Audit Manager
Robert Howes, Senior Auditor
John Piecuch, Senior Auditor
Lena Dietles, Auditor

Appendix III

Report Distribution List

Commissioner N:C
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Director, Field Assistance W:CAR:FA
Director, Strategy and Finance W:S
Chief Counsel CC
National Taxpayer Advocate TA
Director, Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O
Office of Management Controls N:CFO:F:M

Appendix IV

Stakeholder Partnerships, Education, and Communication (SPEC) Field Office Staffing Levels as of February 2002

Territory Office	Number of Employees Required by Plan	Number of Employees as of 02/19/2002		Territory Office	Number of Employees Required by Plan	Number of Employees as of 02/19/2002
FIELD AREA: HARTFORD						
Hartford, CT	12	7		Portland, ME	2	0
Providence, RI	6	0		Albany, NY	11	5
Boston, MA	16	7		Buffalo, NY	12	10
Manchester, NH	7	4		New York, NY	18	12
Burlington, VT	2	0		*Brooklyn, NY	0	6
FIELD AREA: INDIANAPOLIS						
Chicago, IL	17	13		Cincinnati, OH	12	8
*Springfield, IL	0	2		Charleston, WV	4	2
Indianapolis, IN	12	9		Louisville, KY	7	2
Detroit, MI	17	10		Columbus, OH	9	2
Cleveland, OH	14	5		Milwaukee, WI	12	10
FIELD AREA: GREENSBORO, NC						
Washington, DC	20	3		Newark, NJ	15	8
*Guaynabo, PR	0	1		*Springfield, NJ	0	1
Baltimore, MD	12	10		Philadelphia, PA	16	11
Wilmington, DE	4	2		Columbia, SC	12	3
Charlotte, NC	10	0		Pittsburgh, PA	12	10
Greensboro, NC	8	10		Richmond, VA	8	8
Raleigh-Durham, NC	8	0		Norfolk, VA	7	3
FIELD AREA: NEW ORLEANS						
Birmingham, AL	11	5		Jacksonville, FL	10	12
Jackson, AL	3	2		Miami/Ft Laud, FL	15	10
Nashville, TN	7	7		Tampa, FL	16	7
Memphis, TN	8	4		Atlanta, GA	16	12
Little Rock, AR	4	3		New Orleans, LA	13	8

Territory Office	Number of Employees Required by Plan	Number of Employees as of 02/19/2002	Territory Office	Number of Employees Required by Plan	Number of Employees as of 02/19/2002
FIELD AREA: ST. LOUIS					
Minneapolis/St. Paul, MN	11	7	Oklahoma City, OK	11	8
Sioux Falls, SD	2	0	Wichita, KS	3	2
Fargo, ND	2	2	Austin, TX	9	7
*Aberdeen, SD	0	1	San Antonio, TX	9	4
St. Louis, MO	11	14	El Paso, TX	7	4
Kansas City, MO	10	6	Lubbock, TX	4	1
Omaha, NB	7	3	Dallas, TX	16	12
Des Moines, IA	5	1	Houston, TX	14	11
FIELD AREA: PHOENIX					
Phoenix, AZ	12	9	Salt Lake City, UT	7	3
Albuquerque, NM	5	2	Portland, OR	11	7
Denver, CO	12	10	Boise, ID	3	3
Helena, MT	2	2	Seattle, WA	14	11
Cheyenne, WY	2	1	Honolulu, HI	4	2
Las Vegas, NV	8	5	Anchorage, AK	2	2
FIELD AREA: SAN DIEGO					
Los Angeles, CA	20	14	Oakland, CA	15	9
Sacramento, CA	12	4	*Fresno, CA	0	2
San Diego, CA	13	5	San Jose, CA	9	7
*Laguna Niguel, CA	0	3			
TOTALS				697	438

Source: SPEC staffing data February 2002 and the SPEC Design Plan.

** Denotes those 7 field offices added subsequent to the initiation of the SPEC function.*

Shading represents those 6 field offices with no staffing as of February 2002.

Appendix V

Adequacy of Technical Support

Territory Office	Adequate Technical Support? Yes	No		Territory Office	Adequate Technical Support? Yes	No
FIELD AREA: HARTFORD						
Hartford, CT		X		Portland, ME		X
Providence, RI		X		Albany, NY		X
Boston, MA	X			Buffalo, NY		X
Manchester, NH		X		New York, NY	X	
Burlington, VT		X		Brooklyn, NY	X	
FIELD AREA: INDIANAPOLIS						
Chicago, IL	X			Cincinnati, OH		X
Springfield, IL	X			Charleston, WV		X
Indianapolis, IN	X			Louisville, KY		X
Detroit, MI	X			Columbus, OH		X
Cleveland, OH		X		Milwaukee, WI	X	
FIELD AREA: GREENSBORO						
Washington, DC	X			Newark, NJ		X
Guaynabo, PR	X			Springfield, NJ		X
Baltimore, MD	X			Philadelphia, PA	X	
Wilmington, DE	X			Columbia, SC		X
Charlotte, NC		X		Pittsburgh, PA	X	
Greensboro, NC		X		Richmond, VA	X	
Raleigh-Durham, NC		X		Norfolk, VA	X	
FIELD AREA: NEW ORLEANS						
Birmingham, AL		X		Jacksonville, FL	X	
Jackson, AL		X		Miami/Ft Laud, FL	X	
Nashville, TN	X			Tampa, FL		X
Memphis, TN	X			Atlanta, GA	X	
Little Rock, AR	X			New Orleans, LA		X

Territory Office	Adequate Technical Support?			Territory Office	Adequate Technical Support?	
	Yes	No			Yes	No
FIELD AREA: ST. LOUIS						
Minneapolis/St. Paul, MN	X			Oklahoma City, OK	X	
Sioux Falls, SD	X			Wichita, KS	X	
Fargo, ND	X			Austin, TX	X	
Aberdeen, SD	X			San Antonio, TX	X	
St. Louis, MO		X		El Paso, TX	X	
Kansas City, MO		X		Lubbock, TX	X	
Omaha, NB	X			Dallas, TX	X	
Des Moines, IA	X			Houston, TX	X	
FIELD AREA: PHOENIX						
Phoenix, AZ		X		Salt Lake City, UT		X
Albuquerque, NM		X		Portland, OR	X	
Denver, CO		X		Boise, ID	X	
Helena, MT		X		Seattle, WA		X
Cheyenne, WY		X		Honolulu, HI		X
Las Vegas, NV		X		Anchorage, AK		X
FIELD AREA: SAN DIEGO						
Los Angeles, CA		X		Oakland, CA	X	
Sacramento, CA		X		Fresno, CA	X	
San Diego, CA	X			San Jose, CA	X	
Laguna Niguel, CA	X					
TOTALS					43	36

Source: Stakeholder Partnerships, Education, and Communication territory manager responses to a Treasury Inspector General for Tax Administration e-mail survey. Forty-eight territory managers were included in the survey. They oversee a total of 79 offices.

Appendix VI

Management's Response to the Draft Report

COMMISSIONER
WAGE AND INVESTMENT DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

August 29, 2002

RECEIVED
AUG 29 2002

MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

FROM: John M. Dalrymple
Commissioner, Wage and Investment Division

SUBJECT: Draft Audit Report – The Internal Revenue Service Needs to Improve the Pre-Filing Tax Services Provided to Taxpayers (Audit # 200140049)

I reviewed your draft report and appreciate that you acknowledged that the IRS Stakeholder Partnerships, Education, and Communication (SPEC) organization represents a new vision of pre-filing service delivery for the IRS. Rather than continue to rely on direct, resource intensive delivery of IRS products and services to taxpayers, the SPEC Concept of Operations (CONOPS) calls for a transition to a new business model that relies on leveraging the contributions of community groups or coalition-based partnerships in the delivery of pre-filing services. While much of the operational infrastructure necessary to implement and manage this new business model was not in place at stand up[1], significant results have been accomplished since October 2000, when the new organization came into existence.

For example, in FY 2002, SPEC made significant progress in creating the partnerships and infrastructure necessary to execute its new business model. Over 50 national strategic relationships have been established with organizations such as United Way, Points of Light, National League of Cities, Volunteer of America, National Council of La Raza, and Federal Deposit Insurance Corporation. Thousands of local partnerships were forged with social services and nonprofit organizations, schools, businesses, faith-based organizations, and political leaders. In 40 communities across the country, SPEC created partner coalitions where members leveraged pooled resources to assist low-income neighborhoods and families.

To educate and inform taxpayers, SPEC developed a comprehensive product delivery process to effectively manage and distribute 154 products, including 9 newly developed in English and Spanish. These products were used to address a data-driven set of outreach and education objectives specifically designed to address key compliance

[1] The term "stand up" as used in this response refers to the inception of SPEC as part of the Wage and Investment Division effective October 1, 2000.

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related problems identified in cooperation with our Compliance and Research organizations. The impact of these initiatives will be measured in the newly developed set of Balanced Measures and local research projects.

While your report accurately points out that much of the operational infrastructure necessary to implement and manage the new SPEC business model was not in place at stand up, it does not adequately take into account the operational complexities of actually putting the new model into practice. Your audit was conducted from October 2001 to April 2002. Understandably, initiation of a comprehensive review of a new organization 1 year after it was created would identify significant inherited deficiencies. As a result, subsequent events have superseded many of the findings in your report.

The report's central conclusion that the lack of staffing had a negative impact on the numbers of taxpayers assisted is an example. Because the report did not capture accomplishments for the entire fiscal year, it inaccurately shows that the number of taxpayers assisted decreased in FY 2002 relative to the past 2 years. In fact, so far in FY 2002 SPEC has already assisted more taxpayers than in FY 2001 with fewer resources, which indicates that we are using available resources more effectively. Similarly, ongoing developments show our operational capabilities, such as information management systems, performance measures, and training programs are improving.

Upon stand up, SPEC inherited many legacy programs that they had to deliver during the 2001 filing season. These legacy programs included the Volunteer Income Tax Assistance (VITA) program, the Tax Counseling for the Elderly (TCE) program, and educational programs, such as Practitioner Workshops, Understanding Taxes, and the Banks, Post Office, and Library Program. Due to the emphasis on successfully delivering legacy programs, the SPEC organization could not start its migration to the new leveraged business model. In FY 2002, the SPEC organization realized substantial improvements in efficiency and effectiveness. We provided assistance and education to significantly more taxpayers than in FY 2001, while at the same time reducing the number of Compliance details by more than 67 percent. In fact, when you consider the reduction in compliance support, we actually served more taxpayers with less staffing resources than at stand up. These efficiencies demonstrate that the SPEC business model is working, and we expect this trend of serving more taxpayers with less IRS resources to continue as SPEC matures.

I am convinced that SPEC's CONOPS is the appropriate strategy for achieving the pre-filing goal of positively influencing voluntary compliance by assisting and educating W&I taxpayers. Surveys show that qualitatively, taxpayers and partners are extremely pleased with the service and support they received in the 2002 filing season. Partner and taxpayer satisfaction received ratings of 4.1 and 4.8 respectively on a 5 point scale.

We have significant work to accomplish in building and refining the operational infrastructure, but I support SPEC's priorities and their plan to achieve them.

My comments on each of the four operational deficiencies noted in your report follow:

1. SPEC Field Offices Lacked Adequate Staffing and Managerial Oversight

Even though the IRS Modernization Design Plan recommended staffing levels, the SPEC management team decided to partially staff field offices until the leveraged business model matured to reflect future business operations. We did not fill some territory manager positions because with fewer employees, the need for them was substantially lower than anticipated in the design plan. This was not because the individuals applying for the positions lacked the necessary qualifications as stated in your report.

Now that SPEC has developed its leveraged business model, we are planning to add 97 employees, including 2-3 additional Territory Managers. We anticipate these employees will be on-board before October 1, 2002.

2. Employees in Field Offices Had Not Received Mission Critical Training and/or Had Not Met Professional Requirements

Our commitment to deliver legacy programs during the 2001 filing season used all of SPEC's resources and delayed SPEC's efforts to start training its employees in courses identified as mission critical. During FY 2002, SPEC assigned training development and oversight to one of its executives as a major infrastructure project. This executive devoted much of her time to identifying mission critical courses, developing course material, and scheduling courses when they would not jeopardize filing season commitments. SPEC will train most of its employees in these mission critical courses before December 2002.

The following are the entry-level accounting requirements of SPEC Tax Specialists:

- GS-5/7/9, 6 hours
- GS-11/12/13, 12 hours

As of the date of this report, 80 percent of SPEC's Tax Specialists have completed their accounting requirements, and the remaining tax specialists are enrolled in accounting classes.

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3. Computer Equipment Was Not Adequate to Support IRS' Volunteer Tax Assistance Programs

SPEC recognizes that budget constraints will never permit the purchase of sufficient computers to adequately respond to the demand of its volunteer tax assistance programs. However, under its leveraged business model, SPEC is identifying external partners who are interested in serving low-income citizens and who can supply computer resources. Examples of these external partners include high schools and universities that have provided their computer labs for VITA sites. Community coalitions of non-profit organizations and community action agencies are also providing computers for use at VITA sites.

During the 2002 filing season, SPEC's VITA program e-filed 80 percent of the returns prepared at their sites, and the TCE program e-filed 43 percent of the returns prepared at their sites. These percentages are significant increases over prior years.

4. Performance Management Systems Had Not Been Developed to Monitor and Measure the Impact SPEC Activities Have On Improving Tax Compliance

For FY 2003, SPEC developed five business objectives, which we will closely monitor and measure to determine the impact of educational efforts on changing taxpayer behavior. We will use local research projects to baseline existing compliance behavior and the impact of specific outreach activity. SPEC will use the results to perfect a model that accurately measures the effectiveness of educational efforts and considers external influences.[2] SPEC also developed 11 balanced measures that assess business results, taxpayer and partner satisfaction, and employee satisfaction. These measures will provide additional information on SPEC's success in achieving its business objectives.

In the relatively short timeframe since stand up, SPEC has made substantial progress in addressing the operational deficiencies you identified. If you have any questions, please call me at (202) 622-6860, or Mark Pursley, Director, SPEC, at (404) 338-7104.

[2] External influences include tax law changes, state of the economy and socioeconomic factors.